Westpac Banking Corporation

2007 Interim Results
Analyst Briefing

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TRANSCRIPT

Andrew Bowden, Head of Investor Relations:

Good morning and welcome to the presentation of Westpac's first-half result in 2007. My name is Andrew Bowden and I'm responsible for Investor Relations.

In addition to those here I would also like to welcome those that have dialled in on our conference call and those that have logged in on the website. The format for this morning will be very similar to prior presentations. David Morgan our CEO will open up and provide some opening remarks as well as provide an outlook and Phil Coffey our Chief Financial Officer will do the details of the result. We will then open the floor up for questions.

Before commencing though could I please remind you all to turn off your mobile phones. Without further ado let me introduce David Morgan to present his 17th Westpac result.

David Morgan, Chief Executive Officer:

Thanks Andrew. Good morning and welcome to our first morning presentation for analysts and investors. We hope that might help you get home a little earlier tonight.

I'm delighted to present another record profit for Westpac. This was a high quality result; we delivered solid earnings' growth, we further increased our leading return on equity and it was a sustainable result as evidenced by increased momentum over the prior period, full provisioning for the credit environment and the absence of material one-off impacts.

There has been a noticeable shift in the composition of our spending. We have deliberately shifted investment to businesses that have a higher growth trajectory and to sectors experiencing strong market conditions, particularly well in business banking. That shift is beginning to pay off. We've achieved this notwithstanding that we have some challenges, particularly in New Zealand. We have put in place steps, particularly the appointment of Brad Cooper to execute the turnaround and we are confident of success.

This was another characteristic Westpac performance of double digit earnings' growth and increased return on equity. Cash earnings per share were up eleven per cent. Economic profit the best single financial measure of the value created for shareholders was up 13 per cent. At 24 per cent our return on equity stacks up well against the leading banks in the world. This was a particularly good outcome given the strong growth that we've achieved in this period.

We also cut a further 90 basis points off our cost to income ratio to under 46 per cent and we've returned that value to shareholders. We've increased the dividend by 13 per cent, reflecting our confidence in the outlook.

I use the term 'characteristic' to describe this performance because it builds on the consistency of growth and return that have been the hallmark of Westpac over the last eight years. This aligns with how we run the company, not for any single reporting period, but for long-term sustainable performance.

When this company runs well it's not because of the performance of any single business unit, it's a balanced performance across all our businesses. In the last 12 months we've grown our balance sheet broadly in line with systems. That is something no other major bank has been able to achieve.

Our Australian Consumer segment has maintained its momentum delivering an improved 12 per cent growth in cash earnings. We've made some big investments in our Australian Business segment and these are paying off, with cash earnings also up 12 per cent.

The Institutional bank performance was similarly strong up 12 per cent, but the more impressive 17 per cent growth excluding the largely discontinued structured finance business.

BT delivered a great performance growing market share in a fast growing market. The Australian wealth segment is the fourth largest private pension market in the world and one of the fastest growing of any financial services segment. Moreover, it is plainly an opportunity right here in our own backyard.

BT cash earnings increased 22 per cent over the year; BT is exceeding our expectations. We bought well, we integrated well; it's delivering a return on equity of 21 per cent. Our wealth business is now contributing 12 per cent of group earnings, up from five per cent in 2002.

As previously mentioned the New Zealand business remains our longer-term turnaround challenge. While achieving a six per cent growth in core earnings, higher impairment losses resulted in a decline in cash earnings of three per cent.

Our strategy remains unchanged. We continue to focus on our core markets where we have a strong knowledge and a proven comparative advantage. We've aggressively tapped the growth opportunities inherent in our markets, including increasing our investment in wealth to capture superannuation flows, capitalising on the corporate regearing that's currently taking place and diverting more resources to Queensland and Western Australia.

In 2006 we made a number of changes to improve our growth orientation and we are now seeing the benefits of those changes. We've opened more branches, more business banking centres and employed 400 more people in the front line, and we're not stopping there.

Importantly, we've maintained our discipline. Funding investment with productivity gains and fully provisioning for the credit environment.

We've been at the forefront of corporate responsibility and sustainability and this continues to be reflected in our leading global position. This position has really engaged our staff contributing strongly to high employee commitment and low turnover and further strengthened our employment brand. Those are great assets at any time, but particularly at a time of zero unemployment in the financial services sector.

One of the outcomes of the solid earnings growth and the high return on equity is that we continue to generate significant shareholder value. This value is being returned to shareholders with a 13 per cent uplift in dividends.

So to summarise, the key points from this result that please me most are the solid earnings per share growth, the leading return on equity and the quality and the sustainability of the result as evidenced by momentum, full provisioning and the absence of material one-offs.

Let me hand over to Phil Coffey to discuss the details.

Philip Coffey, Chief Financial Officer:

Thanks David and good morning everyone. Let me start by saying how pleased I am to be delivering such a simple set of financials.

In looking at the composition of the result it was a textbook performance; strong revenue growth with a disciplined expense performance, generating a healthy gap between our revenue and expense growth or a healthy 'jaws'.

We saw an increase in impairments, but at a rate expected given the growth in lending and given the current economic settings in Australia and New Zealand and we had a return to a more normal tax rate.

When you look at this slide importantly I think you can also see that the picture of revenue-driven growth is true whether we look at the performance over a 12-month comparison or in comparison with the prior period.

But not only was our revenue-driven performance based on that revenue, but it was of a high quality. We've had the inevitable one-offs over the last three halves and I can refer to the credit card accrual from last year and of the impact of FX translation and hedging over the prior two halves.

But if you look at their overall impact it doesn't detract from the quality of our performance so if you back out those effects you will see that our underlying revenue growth is a healthy eight per cent over the 12 months and six per cent over the immediate prior half.

A major driver of our revenue has been our strong balance sheet growth, with loans up 17 per cent and deposits up 15 per cent. This slide pretty much sums up our performance in Australia in terms of the balance sheet. At the top of the slide you can see that over the last 12 months we've maintained the momentum that we restored in 2006 and we've held total growth in line with system.

And that performance has been broad based, and that's what you can see in the bottom part of this chart, where you can see the growth performance against various markets and segments. I think these charts highlight that no other major bank has matched the breadth of our performance and the breadth of our growth. And that's a pretty good outcome in a competitive market.

Growth in line with system has been delivered with margin compression close to what we expected. And, the combined asset and liabilities spread mix impact in BCB and New Zealand was 8 basis points over the year.

One of the more significant factors influencing margins has been the strong growth in our Institutional bank lending. By increasing the proportion of lower spread Institutional bank loans, we have a mix impact that's contributed 3.5 basis points to the reduction in overall margins over the year. It is worth noting though that the absolute spread on Institutional loans has really changed very little over a half or over the 12 months.

At our result announcement last year we explained that the 219 basis point margin for the second half of 2006 wasn't really the right starting point to consider our margins going forward. And you can see in the right hand part of this slide that the benefit of a return to high Treasury interest income and the correction of the credit cards impact has contributed to the overall margin rebounding to an overall level of 225 basis points in the last half.

If we look at margins in a little more detail, the decline we experienced is due almost exclusively to the asset side of the balance sheet; to both spread and mix effects there. When we look at those assets - the growth in mortgages, which has been strong, coupled with the sheer size of the portfolio, which today is $117 billion, has had a mix effect on our spreads.

We've also had a noticeable impact from high growth in fixed rate lending, particularly in Australia where our fixed rate portfolio as a percent of the total increased four percentage points over the year. the increase in our low rate cards and lower rate balance transfers has also contributed to a reduction in spreads and the rapid growth overall in our balance sheet has had that front book/back book impact on our margins as well.

On the liability side, the zero overall impact masks an eight basis point improvement in deposit spreads that were offset by a mix impact of a similar order. And the mix effect is mostly due to the rate of growth in the lower margin online deposit accounts, particularly in New Zealand. Non interest income growth was solid over the year, with BT non interest income, in particular, up 17%. And both BCB and WIB non-interest income benefiting from higher customer activity.

In the Institutional bank this has included higher transaction fees and a stronger debt market earnings. BCB benefited from the prior period fee changes that we saw last year. When we look at growth over the 12 months the sale of Master Card contributed $21 million to revenue. Although this was offset by lower trading income after the exceptional performance we saw in the first half of '06. Growth over the past six months has been a little more modest, and that's to do with the realignment of our transactional fee structures in New Zealand, the cost of New Zealand hedging, and the high SCG earnings that we had in the second half of '06 and all of those factors have reduced our reported growth rate.

Turning to expenses. We have maintained our traditional disciplines in the expense area, and our revenue growth has been significantly higher than our expense growth, leading to a 90 basis point drop in our cost income ratio to just under 46%. Our banking cost income ratio dropped 130 basis points, and is now below 45%. We achieved that efficiency improvement whilst we've been investing more in our high growth areas in wealth and in business banking.

At a headline rate we recorded just over 4% cost growth for the year and 3% cost growth over the half. However, if we back out the exchange rate impacts, that cost growth underlying looks more like 4% over the year, and 2% over the half. So given the strong activity and the investment that we are supporting, that cost growth profile of 5% over a year and 2% over the most recent half is one we feel very comfortable with.

In 2006 we spent some time discussing how we were adjusting our cost profile more towards revenue growth. And this slide depicts how some of those decisions are playing out. The chart on the left disaggregates our major project spending into four distinct categories, and you can see from the slide that following the completion of a number of our large infrastructure projects that took place last year, our resources are now being diverted more towards front office related initiatives, and we've had some small increase in our compliance spending.

So we've not scaled back our overall spending, but we are investing more in smaller projects that have a greater orientation towards revenue growth. And they're things like our more automated credit card origination platform and our foreign exchange systems.

I should note that this slide only picks up our major project investment. And much more of our front office costs are in fact captured in the business units in the form of higher personnel expenses and other operating expenses.

Our impairment losses were up 25%. But that was a level not unexpected given the 17% growth in our loan book, and the current economic settings. And we are coming off a very low bad debt charge that we incurred over 2006. In fact, the ratio of our impairments to average loans is still below the historical average levels. In arriving at our higher impairment losses, you can see it's been driven by increased collectively assessed provisions, but also lower new individually assessed provisions.

We've also had a significant reduction in the benefit that we get from recoveries and write-backs over the year. In breaking down that $62 million increase in our collectively assessed provision, you'll see $51 million was due to growth in the balance sheet, and the majority of that was related to our credit card growth. $11 million is mainly due to high delinquencies in Australia and New Zealand, and that was offset by some improvements in WIB.

For some time we've been talking about how the changes in the operating environment will flow through into impairment losses under AIFRS. And we can see that in the latest half where higher interest rates and exchange rates in both Australia and New Zealand have contributed to higher bankruptcies, a rise in delinquencies and in New Zealand, some regrading of our business exposures. In addition, we've seen increased tensions in the Pacific, particularly in Fiji and in Tonga. So given these conditions, our provisioning cover has increased and the collective provisions to non-housing loans has risen five basis points to 114 basis points.

In responding to those trends, we've also invested in risk mitigants. That includes in enhancing our analytics so that we can better identify stress earlier, particularly in our consumer portfolios. We've also increased our collections resources, and they're now 17% higher than they were a year ago. And the introduction of Basel II has also further increased our business intelligence, which we were able to apply to the management of the credit risk in our overall portfolio.

When we look forward, with interest rates expected to stay at least around these levels, and given that overall impact on the environment, we expect a similar trend to our impairment losses to the one we experienced in the first half of the year; so that's moderate growth in new provisions, and little impact from recoveries and write-backs.

The most significant influence on our capital levels has been the opportunity to reinvest in the business. Risk related assets have increased a very high 10% over the past six months, and with a high ROE of 24%, this combination allows us to deliver strong value creation. In discussion with Standard and Poor's over the half it also became apparent that we were being more conservative than required in the treatment of certain capital deductions in relation to investments in the specialised capital group area. And changes to that contributed four basis points to our ACE ratio compared to the prior period. However, that benefit has been more than offset by a number of other items that have gone against us in the half, some of which tend to be self correcting. They have included changes to our deferred tax asset balances and to our foreign currency translation reserve. And those other items reduced our ACE by 19 basis points over the half.

But we have maintained our dividend, the higher dividend payout ratio we indicated last year, and at 6½% for tier one and 4.34% for the ACE ratio, we're comfortably in the mid-part of our target ranges.

So turning to our business units and starting with Consumer.
Our Consumer segment saw really good growth in the fastest growing States of Western Australia and Queensland, and we've diverted resources to those States in 2006, and we're getting the return. On top of the additional head count, our sales have also benefited from the more extensive use of our Reach CRM platform. When looking at the use of third party and in mortgages in particular, broker usage has been relatively flat at 39% over the half.

We had a spread decline of 10 basis points recorded in our mortgage portfolio, including the impact of the faster relative growth in fixed rate lending that I mentioned. This decline was offset by an improved spread of 13 basis points on our deposit products, most of which was recorded in the first half of '06.

Impairment losses grew significantly over the year, and that was in response to the very high growth that we saw in our consumer unsecured portfolio.

If we look in a little more detail at our cards portfolio, it has been a source of strong growth for us over the last two years. But importantly, the majority of that growth has been from our existing customers, where our improved analytics has basically encouraged those customers to shift more of their business to us. New customer acquisition has been tilted towards our low rate cards and to the Virgin products. And this shift, combined with the increased costs of funding interest free periods was largely behind the 76 basis point decline that we saw in card spreads.

The cards portfolio, as I said, experienced increased provisioning, but that was in line with the larger book, and some increase in delinquencies. Looking ahead, we don't expect to see the rate of growth in cards to be maintained, and that's partly reflected in the fact that the one off gains from our existing customers is not going to be repeated.

In the Business segment, as David mentioned, we've been actively pursuing higher growth. And we're really pleased with the additional customer relationships that we have built over the last six months and last 12 months. Reflecting that relationship focus gains have been recorded on both sides of the balance sheet, and you will see that deposit growth at 17% actually exceeds our loan growth of 14%. Much of the lending growth in our Business segment has been recorded in our middle markets customers, and they tend to have larger lower margin facilities. And the impact of that mix has been a major driver of the 13 basis point decline that we saw in business lending spreads. The credit quality in the portfolio remains sound.

Our Institutional bank results were very solid. We saw exceptionally strong growth in lending, as a result of leveraging our close customer relationships and our leading position in debt markets. You can see from the bottom part of that chart that that strategy is working. Get the finance business up front with a view to migrating customers and their business into the capital markets. And the result has seen a significant increase in the revenues from our overall debt market operations over the year.

So while balance sheet lending to larger corporates is a low return in itself, the aggregate relationship returns are very acceptable. And that's from capturing the higher returns from the capital markets business and from transactional banking, and from financial markets hedging. So that success has allowed WIB to absorb the impact of lower revenues from foreign exchange and lower revenues after the sale of our sub-custody business and the run down in our investment securities portfolio. So if we excluded those two latter one-offs, we would have seen Institutional bank revenues closer to 11%.

Our Financial Markets and Treasury businesses continued to deliver solid returns. And they enhanced the value we get from our dealings with customers and from our balance sheet. Now we expect some volatility in earnings because those businesses are impacted by market conditions. But you can see we have good diversification across asset classes, and in the past six months our Capital Markets in our Treasury businesses have benefited from interest rate moves in Australia and New Zealand. While our Foreign Exchange, Energy and Equity businesses have been somewhat quieter. In aggregate, you can see that the most recent half is a good improvement over the immediate prior period, but it's still below the stellar results we saw in the first half of '06. When we look at those businesses and take them together, the result is slightly ahead of our expectations.

BT's performance has been a standout. Excellent fund growth, improving cross-sell and a better insurance performance. And they've contributed to a 22% uplift in cash earnings based on a 14% uplift in revenues. Our insurance performance was particularly positive, with revenue up 22%. And our smaller businesses in Broking and Margin Lending also reported solid growth. And there have been some good signs of improvement in our advice business, where we've backed an additional 85 employees into that group over the year.

Compared to the immediate prior period, BT delivered a 16% uplift in cash earnings. Now we have benefited from buoyant investment markets. However for us, the key feature of the result can be seen in this chart. In the most recent quarter we've gained good market share in both platforms and in investment management. In insurance we've also been successful in improving cross-sell, and that's allowed us to benefit from the solid banking growth as well.

In particular, of the loans our home finance managers originate today, 45% have Westpac Home and Contents insurance. And that's up from 38% in the immediate prior period. Other insurance product cross-sell has also been positive.

Our New Zealand business has been our most challenging. However we are seeing signs of turnaround, with 6% growth in core earnings. But the bottom line however has been impacted by impairment losses increasing and moving back towards longer term norms. Over the half we've made progress in improving our overall competitiveness. We've repositioned our transaction products, and we've moved closer to market in pricing and credit assessment, particularly in mortgages where we were out of step. The changes have led to an improvement in customer volumes, but they've also had a significant impact on margins and on non-interest income growth. Margin decline saw significant drops on both sides of the balance sheet in New Zealand, with the largest contributors being the mix effect of the rapid migration to online deposits, and the spread compression in our cards portfolio.

Impairment losses in New Zealand have picked up, as the economy has begun to feel the strain of the sustained higher interest rates and the strong Kiwi dollar. But when we look at the portfolio we're not seeing any increase in impaired assets or a significant pick up in write offs. What we are seeing are the signs of stress that come through with high delinquencies, in our consumer portfolio, and a number of regrades in Business banking. These changes however only move us back towards more normal levels, after impairment losses have been at very low levels for some time, and I think you can see that on that chart.

And importantly, when we look at the consumer delinquency and the business regrades, they're disbursed widely across the geography and across industry segments. So we're not really seeing any signs of a concentration or systemic issue.

At our full year result last year, we indicated the major factors that were likely to impact our financial results. And little has changed in the operating environment really over the six months, although interest rates are a little higher and credit growth is slightly stronger. If we map what we said last year with what we delivered, there's some small ups and downs, but in aggregate we ended up pretty much as we expected. As we look to the remainder of 2007, those factors look very much the same. Good balance sheet growth, margin compression at the top of the range, solid income growth from BT and WIB.

Expenses will be modestly higher, and impairments will be faster than loan growth, but also controlled. It's worth noting that we don't expect half on half seasonality to have a large impact.

Thank you. Now let me hand back to David for his summary.

David Morgan, Chief Executive Officer

Thanks Phil. Let me turn to the outlook. The Australian economy remains in good shape with continued expansion despite the ongoing impacts of the drought. Inflation continues to be quite remarkably well behaved, which means that interest rates are likely to remain steady for the rest of the year.

By contrast we expect a period of slower growth in New Zealand, reflecting both high real interest rates and a high exchange rate.

In Australia, overall credit growth in the year to March '07 was 15%. This growth rate is expected to be broadly maintained through to the end of calendar '07. Average business credit growth is expected to be around 16%. Average household credit growth is expected to be around 14% by December '07. In New Zealand, we expect total average credit growth to come back from around 14% to around 12% in December '07.

Looking at the outlook for household savings, superannuation is clearly already the dominant form of personal savings. And in volume terms, is almost double savings in bank deposits. Moreover, superannuation is expected to grow materially above the rate of bank deposit growth. We're very well positioned to capitalise on this profound and accelerating shift in the composition of household savings.

In the coming six months the key priorities I've set for the bank reflect distinct and targeted strategic choices, particularly with respect to wealth management and business banking.

Firstly, wealth management in Australia. This is a massive opportunity and we are actively and aggressively growing our share. Our platforms are already sector leading. In cross-sell we've only just scratched the surface, but this is an opportunity we will not miss. We're also tapping into the superannuation revolution by creating new investment product. In particular, our specialised group in Hastings are tapping into the infrastructure funds opportunities.

Secondly, Business Financial Services under our new Group Executive Peter Hanlon, where we're capitalising on our expanded personnel, increased footprint and improved processes. At the same time our sector leading online corporate payments capability promises a further leg to the growth.

Thirdly, New Zealand, where Brad Cooper will be executing the turnaround, building on the product repositioning that's already been put in place, focusing on the fastest growing Auckland market, while protecting our South Island heartland. We're well positioned to deliver a strong 2007 through a combination of solid earnings growth, leading return on equity and high quality sustainable performance. We have an excellent franchise and a refreshed executive team.

In conclusion, I'm very positive about the outlook for Westpac. Thank you and Phil and I would now be happy to take your questions.

Question & Answer

Ross Brown, Deutsche Bank

I just wanted to challenge one of your comments David, around the volume growth, you know being the fastest growth in a number of products relative to your big bank peers. Because you're right, that's true, but if you look at the product spreads change particularly in the last half, mortgage spreads fell five basis points, which would have effectively offset the volume growth. Card spreads were down 70 points, which would have offset the volume growth.

I was just wondering to the extent to which you were satisfied that the volume growth has purely been driven by price, and actually that's not a great indicator of the franchise performance?

David Morgan

Thanks Ross. Firstly, we do need to focus on the underlying decline in margin and spread. As you know, there's a lot of noise there, particularly with IFRS. Secondly, the spread and margin decline is exactly in line with our expectations. Thirdly, if you look at our spread and margin decline over a two year period, it is absolutely in line with our peers. Fourthly, if you are growing faster than your peers, then there is a quiet mechanical aspect in which your margin contraction will be slightly higher because you've got a higher proportion in your front book than your back book.

But lastly, I presume the question is fundamentally going to the profitability of our growth. And while we've produced this growth, we've also increased our return on equity. And we not only increased it relative to our history but it is the leading return on equity in the sector. So in terms of the fundamental measure is this profitable growth, the facts are it is.

Ross Brown

I guess I'm being a bit more specific rather than the total group spread margin. I'm talking more around the consumer bank in Australia where you have had very significant spread pressure, and it looks like more spread pressure on a product basis than the competition. And yet you've had better volume growth. But really is that, on those products, cards and home lending, is that actually a satisfactory outcome? Because the offsets come on deposits where you've had spread expansion, but you're pricing in a number of products on deposit look now uncompetitive online CMAs.

I'm just wondering whether you are happy with those trends across the deposit and the consumer bank in Australia, because they do look like volume at the expense of price?

Mike Pratt, Group Executive Business Financial Services

Perhaps I’ll pick that up. Ross, first of all on mortgages. If you look at year on year, spread compression is 10 basis points. Half on half it’s four. So we’ve actually improved our position in the second half, and that’s by really focusing in on a number of different issues, particularly in the third party channels. So it’s actually improving position half on half if you look at what we’ve done. And yet volume has actually improved in the second half. So it’s actually quite counter to what you’re suggesting’ if you look at a half on half position.

In the cards book, that’s largely around the mix issue, particularly into low rate. And that compression there is certainly reflecting that significant mix change. What you’ll find going forward though, which Phil mentioned in his presentation, is that you won’t see that growth occurring to the extent it has over the past 12 months. The growth really has been around 60% in our own portfolio, 40% in terms of new to Westpac customers, including Virgin.

So they’re the issues in the cards portfolio. The big book though of mortgages, $117 billion, is actually improving in terms of spread and better growth; so I’m very happy with that performance.

Ross Brown

[inaudible]

Mike Pratt

Okay, well perhaps I can get with you afterwards and we’ll go through the detail of the numbers, but it’s actually improving half on half.

David Morgan

It’s just a rounding issue Ross, and I know you’re referring to the spreads in the ASX.

James Freeman, Goldman Sachs JBWere

I was just hoping to actually get a bit more clarity on how much of the trading income in the non-interest income was actually relating to proprietary business rather than clients? I mean you’ve given us the Treasury profit, which have no non interest income but I'm just wondering when you go to the non-interest income line you’ve got the trading profits in there, I'm just wondering how much of that is proprietary versus client?

David Morgan

We don’t run a big ‘prop’ trading activity. I mean we’ve got basically aspects of teams in our financial markets who really, their positions are generally created by the facilitation of customer activity. Now they’ve got risk limits in which they can operate to manage those flows, but we don’t have, in the traditional investment bank sense, a group of people sitting quite isolated operating as a prop trading desk. We don’t have that.

Matt Davison, Merrill Lynch

I had another question on the return profile I guess. If we look at your profit growth that was 11% year on year and risk weighted asset growth at around 17%; and if we look at the Institutional business you’ve had 40% growth in loans and acceptances, and around 11% revenue growth when we look at it on an adjusted basis.

Can you give us a bit of colour on just how these trends will converge in coming halves particularly with relation to feed growth and the specialist capital unit as well within WIB?

David Morgan

Phil, I might ask you to pick up on the WIB issue. Certainly in the Specialised Capital Group, particular under IFRS, there are different rules on which you can bring income to account, and we’ve got a number of deals in the pipeline that we’ll be completing in the second half, but you’ll see a material pickup in the revenue from Specialised Capital Group in the second half. Phil, do you want to pick up the other aspects of the second half in WIB?

Philip Chronican Group Executive Westpac Institutional Bank

Obviously the loan growth and the WIB business was very strong and I think it would be fair to say it wasn’t necessarily in line with where we would have planned the business. But as Phil Coffey pointed out in the presentation, when you get closer to your customers and trying to go alongside with them and partner with them in their transactions and corporate customers have been more active over the half, in fact over the last 12 months than they have been for a number of years previously, that's given us the opportunity to be beside them, underwrite their activities, be they acquisitions or new investments.

We're not expecting that rate of growth to continue because as Phil articulated, that's all part of a continuum of how to move that through to the capital markets. So this is a snapshot at a point in time but it's certainly not a rate of growth that we would expect or indeed plan to have continue into the future. What we're looking to do though is to maintain the very strong flow through we have through the syndicated loan market, the asset back securities market and the Australian bond market. In the investor discussion pack that's also available for distribution you can get a good sense of where we're positioned in those markets.

Jeff Emmanuel, UBS

Firstly Phil, congrats on the disclosure, very simple straightforward and a lot more clarity in there in terms of the understanding. David, a couple of questions, firstly on your revenue lines. You have great growth in net interest income and the balance sheet really sitting behind that. I'm just wondering, fee income didn't seem to sort of keep up. I'm just wondering if that's just a timing thing or is there something more behind that? Then I've got a second question.

David Morgan

Okay. As far as the WIB contribution, Jeff, it's partly a timing issue there. SCG, which has been a very big contributor in the previous half and was materially down on that. As I've said, because of when you can bring this to account it's certainly that we'll bring it through in the second half.

Phil, can you take us through the detail of some of the other non-interest income?

Philip Coffey

I think the non-interest income story on fees actually is that going forward, whilst you might get for every loan more of that income actually now going to be showing up in your net interest income line, because more of those fees are actually amortised through net interest as opposed to turning up as a straight fee and crystallised at that point in time.

Jeff Emmanuel

Secondly if I could ask, on page 28 of the profit statement you put up some interesting detail on your credit quality. Just a system question more than anything but other consumer and mortgages at 90 days past due over a per cent now on consumer, 0.29% on mortgages, they've just gone up above the 10 year historical average. I'm just wondering if that's concerning you guys and whether this is really the beginning of a longer term trend in the credit cycle?

David Morgan

Jeff, this is completely consistent with our models, with all our models in the other consumer – it's absolutely consistent with what you'd expect from the cumulative impact of the interest rate hikes that we've had both here and in New Zealand. So where these were expected, they're predicted and we believe our models are robust there.

Jeff Emmanuel

No concerns David -?

David Morgan

No concerns Jeff, given the robustness of our models. Now they're as good as your macro-economic assumptions. We still believe that unsecured consumer credit is the hardest risk part of our book, and the systems book. But we also believe that to get a really material kick there really requires the unemployment rate, additional increases in interest rates will have a modest and predictable uptake, but it's really around the unemployment rate.

And in terms of the outlook that we can see in our core economies that's still holding up very strongly.

Craig Williams, Citigroup

A somewhat related question to Jeff's second question, just in terms of trying to comprehend bad debt provisioning under IFRS accounting. We not in this half you've seen rising delinquencies, your volumes growth has been very strong in your consumer book in Australia. I think you've noted within the pack that the bulk of individually assessed provision reduction in the year has actually been in the

WIB business. I suppose I'm trying to understand why the bad debt charge for a consumer book in Australia actually went down half on half? I understand year on year there's been quite good growth, but the half on half movement?

David Morgan In effect in the way that our models work some of that impairment expectation was put through in our models in the second half of 06 and so it doesn't lead to the straight path through into the next half. I noticed that as well Craig, when I was looking at it. But it effectively I think – the way I look at it, we will over the way if this pans out actually get more early into our impaireds and then when those delinquencies crystallise, as long as they come through as our models expected, then you won't necessarily get a pick up at that point in time. The only pick up you'll get is if they perform worse than what you've expected in your models.

Craig Williams The BT or the wealth funds growth of I think it was 6% year on year, the market share trends look quite positive, the market movements have been very good during the period but the fund growth was about 6%, it seems low relatively. Can you explain that please?

Rob Coombe Group Executive BT Financial Group Early on in the year there was a fairly substantial, over a billion dollar fixed income mandate redemption from the book. We substituted that with much higher margin business into our Australian equities business throughout the course of the year. So I think I'd encourage you to look at a couple of things; one is the market flow or market share analysis in the last quarter, which is very strong. And also the growth in funds under management in the second half of the year has been very strong as well.

I might also add, we manage a balanced book of business here, so whilst the Aussie market's up 20%, as we know the international market's been flat over the past 12 months, so we really benchmark returns to like a balanced fund, which is around the 10 - 11% mark.

Brian Johnson, JPMorgan Phil, everyone's saying the disclosures are better but I want to review what I said at the last result, which is kind of a compliment. It's more of a negative not compliment. But it's a hard gig when your margin goes down and you get hammered by the analysts, and when it goes up you get hammered.

My question was, a few weeks ago up in Hong Kong, you very kindly put up a revenue growth target, which when you crunch it out works out to be 7.5% on the low side, 9.5% on the upside if you go through and weight all the businesses. Previously the cost growth target was kind of this 4% to 5%. My question is, given those targets were recently given, but I can't see them specifically enunciated today, is it fair to say that they still hold true?

David Morgan Yes, it is.

Andrew Bowden Can I just say, David, they are in the discussion pack.

David Morgan Yes, there is an IDP, Brian, that you won't have had a chance to catch up with yet, and absolutely we reproduce them there.

Brian Johnson And they are medium term?

David Morgan I think there's one subtle word you used there which was 'target', and I think what we've given you is an indication of the range of possibilities for us that we see in that market in terms of revenue growth. Whereas I note some other institutions will explicitly come out and say there's a target revenue growth, we're indicating why we're positive about revenue growth given those opportunities. But we're not sitting out there with a target.

Brian Johnson My second question, David, and I apologise, this is a question I've asked before; but if you have a look at something that I've always felt kind of differentiated Westpac is that you guys have been spending about half a billion dollars up above the line as basically opex spend, and you're targeting apparently four to 5% cost growth. Now if you have a look at the other banks, you've got ANZ saying five to seven, they've obviously got a big kind of push into retail banking; you've got NAB that are saying sub-inflation but they managed to sock away 900 million bucks last year and their cost did gap up 10%, so I think they can be excused for having stuffed it up and a little bit of benefit coming through. But then if you have a look at Commonwealth Bank, Commonwealth Bank are basically saying 4% to 5%.

Now all of that sounds good, yours is in line, but the fact is that you've actually spent I'm guessing, about two and a half billion dollars building these platforms. Why is your cost growth running at peers? I mean if you think about it, if these great automation benefits are coming through it's hard not to conclude that the two and a half billion dollars that have been spent, the incremental efficiency return doesn't seem to be there. Can you run us through why the cost growth – I'm not interested in the mechanics of spending on this and that, but what I'm interested in is where's the incremental return on the two and a half billion dollars of opex which, after all, is about 25% of the shareholder funds?

David Morgan Brian, in terms of the cost benefits of the major programs, and Pinnacle was probably the major program where we were looking for predominantly a cost benefit. We got those savings, we got them a little later than we expected, but we basically got the savings out of those.

For a number of the other platforms we were looking predominantly around Reach, around Corporate Online, we were looking for a revenue benefit. And part of the reason that you're now seeing our good pickup in our share growth is as these platforms start to produce those revenue benefits. So if there's a learning for us out of this in terms of communication with the market, it's possibly greater clarity around where we were seeing the NPV of these in terms of a cost reduction vis a vis a revenue uplift. By and large they are delivering in line with what we're looking for.

Philip Coffey Can I just add a couple of comments, one is obviously we're still seeing healthy growth in our amortisation so whilst it hasn't picked up half on half we're still carrying a $90 million odd expense, which is the processing of those spends.

Brian Johnson It's going down from this point though, isn't it?

Philip Coffey Well we're close to the peak but as we keep the expense growth, investment growth around the same levels, it's not going to sort of suddenly taper off. You heard me talk about how we're orientating that towards more front office staff.

The second thing is you've seen us grow loans by 17%, deposits by 15%...

Brian Johnson Not good enough Phil.

Philip Coffey But we're processing all of that activity – we're processing it and we're maintaining expense growth between four and five. There are major productivity benefits that we are delivering on right now. If we hadn't made those investments, if we hadn't improved our straight through processing etc, you've seen how much growth we've had in wealth, there's no way we'd be able to accommodate those with the kind of growth rates we're getting.

I think as David said, the investment has both been on revenue and expenses, but it's also allowed us to cope with the kind of growth that we're getting right now without seeing an expense bubble.

David Morgan And the additional investment in frontline staff as well Brian. We've been using that dividend to fund that investment particularly, but not only in Business banking but also in our wealth advisory sales force as well.

Brian Johnson Can I push my luck with one final question. If you go back to 1992, I remember in 1991 meeting with Westpac and thought, oh …. Brian, you can never lose money on commercial property. Now I'd remind everyone that in 1992 Westpac did lose quite a bit of money on commercial property. You weren't the CEO then David. But if you actually have a look at it the great thing about long run averages is every year that it's below the average kind of suggests there may well be a year where it's above the average.

If you have a look at the Australian business products, the eight year historic arrears rate is 89 basis points, it's running at 61, it peaked at from memory, about 250 basis points. If you have a look at it we know the recoveries are declining. David why is this part of the book not where the biggest risk is? If the recoveries are declining, the arrears rate is low, it's well below the eight year rate – and eight years I notice, actually takes out a bit of the really, really bad years – why is that not where most of the risk is given that we also know that underwriting standards in global credit markets are generally declining?

David Morgan Brian, it's actually worth just a brief piece of history around '92. In fact in what we would call today our commercial property book, the losses then were actually quite modest. I mean where we had the massive losses was in the AGC joint ventures; was in a lot of lending to a lot of corporate entrepreneurs; was in a lot of off-shore lending where we had no comparative value, I mean we were the seventh largest corporate lender in America, for God's sake, if you could believe that.

Major lending by AGC in the UK and in Asia, when you really look at our commercial banking business the losses even at that low point and with some pretty awful credit policies and practices, were actually quite modest.

Now today in our corporate property book, as well as being unrecognisable in terms of our credit policies and practices and disciplines, you're just not seeing the supply/demand imbalances in that commercial property book either, as well as just having a lot of, as I say, discipline around covenants and policies.

So it's a good question because credit risk is still the biggest risk in banking and concentrations are what kill you, and properties generally are what does it. I genuinely believe the major risks are not there, they're where I've discussed, but it's a good question and a good reminder never to forget history.

Brett Le Mesurier, Wilson HTM David a question for you; we know you're in a very competitive marketplace but can you comment on the steps that you're taking to prevent ANZ overtaking you in Australian banking?

David Morgan Sure. Brett, if I can just direct you to some facts. If you look at the growth of ANZ in their consumer business around total consumer footings, both on the assets and liabilities side, we grew faster than ANZ. So the gap actually increased over this last period, it didn't narrow at all.

Secondly, I've nominated two investment priorities going forward, around BT and around our business bank. But we also have been undertaking and we'll also certainly be ramping up over the BSR period, the three year (medium term planning) period that we're about to go into, around selected investment, further investment in our Consumer banking footprint. But, as I say, if you look at the facts that gap widened in the last half. It didn't diminish.

Brett Le Mesurier There's also an issue in terms of brand recognition. Are you fighting on that as well?

David Morgan Absolutely and I think you've seen the new brand campaign and you've seen the new brand spend and that is now coming through in brand equity and in customer satisfaction. Mike, if you just want to talk briefly about the effects of that campaign?

Mike Pratt Brett, as you'd be aware, any brand reposition does take time to come through but the encouraging part, we launched that in October, we've now moved from number five of the big five including St George, to number three in brand preference since that launch. That's also now being reflected in the customer satisfaction numbers, which if you look at 12 month rolling, we're now back at number three. And if you look at 12 month compared to the two leading customer satisfaction banks, ,that gap to David's point about footings, is also in terms of improvement, has narrowed a full three percentage points.

So brand is really helping us with that, but overall our customer experience metrics have improved significantly over the period as well. So all of that is leading to growth. It's not just around margin or pricing issues. It's a whole range of things that are improving growth in that segment.

**Nick Selvaratnam
Credit Suisse**

On the subject of capital, notwithstanding your good loan growth, on your own calculations you're mid range on your ace and tier one targets. But moving forward in the Basel II environment, you've got I suppose a slightly more optimistic view as to what the outcomes are likely to be versus some of the other banks. Could you give us your latest thought, bearing in mind there's ongoing dialogue, presumably with the regulators, as to where you see this headed? And if you could give us some idea as to your current thoughts on the magnitude of capital releases and what instruments or how that would be managed on a go forward basis?

David Morgan

Thanks Nick, there is an ongoing dialogue and obviously that will continue. There is no doubt that under the Basel II guidelines, Nick, it is unarguable that the amount of credit risk that we would have to hold against the sort of book that we have would be very material in terms of the capital reductions. What very material – I mean you can easily and conservatively get throughout a 25% reduction in the amount of credit risk capital that you need to hold, and that's conservative, you can get higher numbers there.

The interesting question and more uncharted territory is not around 'will there be that capital release of knowledge in the fullness of time', it's when and how much of that will be required to be redeployed in other risk buckets, notably operational risk. That's a pretty unadvanced art and science Nick. APRA have indicated that the maximum capital reduction in aggregate they'd be thinking about in the short run would be 10%, but one can get potentially larger numbers as everybody gets more comfortable with the regime.

If you look at the amount of economic capital, Nick, that we believe we need to run this company, it is very, very materially below the amount of regulatory capital we're required to hold now, and it's a lot more than 10%. So I think Nick, regulators all around the world including our own will be conservative in the short run but it is absolutely vital if we're to get the benefits of Basel is that regulators do give meaningful capital relief for investment in more sophisticated risk management systems. And if they're not prepared to do that, then that will change the cost benefit calculus for banks. And I've got no doubt that our Regulator understands that and that this is a very material opportunity over the medium term but it will be cautious in the short run. Is that what you're looking for?

Nick Selvaratnam

How would you manage that, by buy backs -?

Andrew Bowden

Sorry, he just asked how would we manage that, would it be by buy backs or other means?

David Morgan

And that will be as always when we're looking at capital decisions Nick, it's how much would we return to shareholders, how much can we profitably reinvest, we invest in our own business. Rob's been managing this relationship, Rob, is there anything you'd like to add to that? Rob Whitfield, our Chief Risk Officer.

**Rob Whitfield
Chief Risk Officer**

No, thanks David, I think you've covered it very well. I mean the thing that is changing in the landscape is that APRA looks to be introducing some flexibility in the timetable, but when they do it – they're still targeting 1 January 2008. Westpac is absolutely still targeting 1 January 2008. But it looks like they may allow some flexibility for some banks and have a more elongated timetable to introduce the Basel II benefits.

Richard Wiles, Morgan Stanley

Phil, last half you put up a slide that said the starting point for margins was 2.27 when you stripped out Treasury and the credit card adjustment. This half you've got a margin of 2.25, so it looks like a very good outcome. However it appears that your non-interest income results were a little bit soft and particularly the trading income result was lower than the strong first half last year. In the Institutional bank it seems that from half to half year differences, transactions have different impacts on that interest income and on-interest income. I'm just wondering if you could give us some indication of the interplay, particularly in the Institutional bank between those two lines and what benefit you might have got in the margin this half relative to the second half of last year?

Philip Coffey

Richard, you're right we said the 2.27 was the right starting point and I indicated that kind of a more normal Treasury outcome would have been four basis points higher. You can see in the chart that we actually ended up at seven. If you think about that, we've had a two basis point absolute decline from 2.27 to 2.25, three extra from Treasury means that the underlying was closer to five. I think that those numbers all pretty much come out as we had been expecting and so that's the way they've played out.

We've also shared with you on that slide both the financial market income, and you can find in the ASX we also showed the split between net and non and most of the financial market's income today is actually in non-interest income. And there's less noise being created by the split there than there has been in the past.

But Treasury will tend to have more of its income in net interest income rather than non-interest income, and it's the non bit that flows through into the trading line. That's why we've provided that breakdown in Treasury as well, so that you can see what's happening in terms of that.

In terms of the impact of WIB transactions on non-interest income, as I mentioned a lump of the fees now get amortised and go up into net interest income. So the real drivers are still going to be some kind of larger transactions where there are fees that you can take because you have extinguished your obligation and therefore you can book it as a fee. There will still be the trading incomes that both are affected, and they're really the major impacts still in terms of our non-interest income coming out of WIB last half. So the second half of 06, SCG had some transactions where there was actually some asset sales as well, and that's another form of non-interest income but that's probably less consistent as an activity that we would expect to see at our SCG. We'd really normally expect to see their growth in fees be a quite regular piece because of the funds under management, and then the other pieces just what transactions have been done and sold down in a period.

Richard Wiles

So Phil, it's fair to say that you've got a three basis point benefit from Treasury in this half relative to the last half – or relative to your expectations?

Philip Coffey

Relative to expectations.

Richard Wiles

There weren't any other major influences on the net interest margin from [indistinct] and his division?

Philip Coffey

No, I can't put my finger on any.

Andrew Hokin, Macquarie

Just a follow on from that Phil, just again on the financial markets income side. You described this half's result as I think a little bit above your expectations and you also described the first half of last year as you did at that time as the stellar figure or stellar result. I guess I just want a little bit more colour on how close you think you can maintain to what you've already described as not far off a stellar result in financial markets?

Philip Coffey

What I actually pointed to was that taken together the results in financial markets and Treasury was slightly ahead of our expectations and I figured I had to do that because there was going to be a question that basically said was this a good result, an okay result, where do we put it – along the same questions that you're coming with, Andrew. So in aggregate those two things were slightly ahead of our expectations and they are still $50 or $60 million below what we saw in the first half of 06.

That I think gives you an idea of just how strong we saw '06. At the time we said '06 actually had trading income almost like $100 million higher than what we expected.

Andrew Hokin I guess just a bit more on that; if I look at that sort of three basis point benefit versus normal that you're talking about there, it seems to me like on an after tax basis Treasury might have been $20-25 million after tax ahead of your expectation, a little bit, not that much. But financial markets $244 versus $256, was it the $256 you said was stellar or was that including the Treasury from first half last year?

Philip Coffey No, it was total trading. There's one other thing; you're kind of looking at the three basis points and saying well that's the total Treasury performance but you're only looking at the net interest income by doing that. That's why we've given you the whole lot, you do need to look at the total because some of it will be in net interest income and have an impact on margins, and some will be in non.

Andrew Bowden I think you actually answered your own question, which is that last year when we talked about the aggregate over performance it was really driven by what we consider to be a very good result in foreign exchange and Treasury, and they were the two contributors to the over performance. If you are looking just at the portion of that slide that is recognised in financial markets, I don't think we would necessarily say that that also was ahead of expectations, I think the ahead of expectations fees is really driven by the again strong Treasury performance piece of it.

Mike Macrow, INVESCO Just on the M&A front, I was wondering if you feel that there are still business that aren't in the hands of the natural holders, what the strategic holds are with your last year in the job, and in particular in superannuation and infrastructure whether you feel that although you're well positioned it's such a huge growth opportunity, is there not an argument to actually do more on the M&A front?

David Morgan Mike, we don't feel we've got any major capability gaps or gaps in our footprint. We certainly do, you're right, see the major opportunity as around in the super on both sides of it, both the gathering side and also the creation of the product side. We're very happy with our acquisition of Hastings there; we're very happy with our organic growth of SCG and we're seeking to organically build up our planner numbers. That's probably the tight constraint Mike, on our growth, it's not around opportunities and our customer base, it's probably around financial planners. Rob, do you want to talk about what you're doing to expand and improve retention and expand our financial planner force which I think is where the biggest opportunity is Mike?

Rob Coombe Yes, there's a few things as David said, we're focused on growing that and building that business rather than acquiring planning businesses. I think there's a lot of risk involved in acquiring planning businesses, particularly holding onto talent after the handcuff period runs out. So what we're doing is building planners internally and we have an employed model internally evolving into a franchise model. So it's a very attractive internal career prospect for the financial planners domestically, sorry, within the bank.

On top of that we've also recently launched a planning or a dealer group, which is targeted to migrating Westpac planners but also targeting the external planners to come and work with us and grow their businesses and to work on our platforms. We launched that about 18 months ago. In that period of time we've gathered about a billion dollars in funds under advice, which makes it the fastest growing dealer group that's been launched into the Australia market. So we're very, very pleased with the way our organic strategy is going.

Jeff Emmanuel, UBS

I actually had a follow up question for Brad Cooper, I know he did the briefing recently but in the press he was quoted as the New Zealand turn around taking 18 months. If I just can get a bit more detail around why it would take that long?

David Morgan

Jeff you know the nature of large retail banks, I mean they're more ocean tankers than they are tug boats. You know as well as anyone in this room about the building blocks you need to put in place and then the slow build on the brand and the customer satisfaction and the footprint and the retention and the cross-sell and the positive word of mouth. Now we put in place some foundations there, we quite sharply repositioned our products, we think we've gone through most of the repricing of our back book, the repricing of our fixed loan book, where we didn't participate we've gone through that pain of the repricing, we repriced our transaction products, we've migrated our customers quite aggressively into the online proposition, which is the right thing for them but involves some short term pain.

So I think we've put some foundations in place including increasing the Auckland's region footprint. I think now the hard grind of execution. And I think Brad's background both out of GE around all of the disciplines around all of the operating system and the process chain and his experience in Six Sigma will help free up costs to invest in the front end. About his experience in an even more competitive market in the UK financial services, particularly when he didn't start with a branch footprint and new mortgages written at 60 basis points. I think it's largely an execution challenge, I think he'll be successful but I don't think on the consumer side, Jeff, which is our real challenge we can or should over promise there.

Rest assured, I'm pushing him for a quicker timetable but he's only been here a few weeks. The business side is actually in pretty good shape, Jeff, and that's where we've had increase in the impairment losses but they were from a truly exceptional low base. And, as I think Phil alluded to, it's around regrading rather than actual losses and we've got the leading market share and it will market an SME and that franchise is in pretty good shape. So it's actually the consumer. But we will be pushing to make it sooner rather than later, I think we just need to give him a little time to get his feet under the desk.

Brian Johnson, JP Morgan

I don't think this result's really significant because BT is bigger than New Zealand and everyone seems to obsess about New Zealand. We know that wealth management structure has got a very strong growth rate but the converse is that you're telling us New Zealand is a great turnaround story – not great, I'll take that as a turnaround story – but if I have a look on your slides today, which are a reiteration of what you said in Hong Kong, BT Financial Group you're saying that expect funds management and distribution to grow at 12 to 15% revenue growth over the medium term, insurance 12% to 14%. Then we go down to the bottom, New Zealand and Pacific banking you're saying five to seven, and the focus in New Zealand is to drive efficiency. That doesn't really sound much like a turnaround story. Could we get some clarification on which is going to be the more important driver in incremental earnings growth going forward? On the slides it would appear that it's BT, not New Zealand, and it's a big gap between the two.

David Morgan

Yes, absolutely Brian. I think that was a real milestone, for BT from nothing, 5% of our earnings to our wealth division to 12% now and larger than New Zealand Brian, you're right. You're right to quote those numbers and we've got faith in those. So this increase in the share of our wealth division is going to go on at least at the rate that I think it's gone on and probably more so over the past five years.

And secondly, New Zealand, you just have to be realistic about the opportunity. I mean again you are right, it is a lower revenue opportunity there, it's a lower growth economy, it's a more brittle economy, it does not have the same wealth management opportunity that we have here and you need to be realistic about what the revenue opportunity is, and then work very hard on every other line including your cost line.

So Brian your inference is exactly right and you can't talk about them in the same breath. One is a real growth story; the other is managing for proper and efficient growth.

Andrew Bowden:

Thank you all very much for attending and good afternoon

[END OF TRANSCRIPT]